

3 May 2017 10:32 BST

Company Note | Estimate Changes

Oil &amp; Gas

**PLAINTIFF'S  
EXHIBIT**CASE  
NO.EXHIBIT  
NO.

9

**ATLANTIC  
EQUITIES**

Neutral

Price Target \$72.00

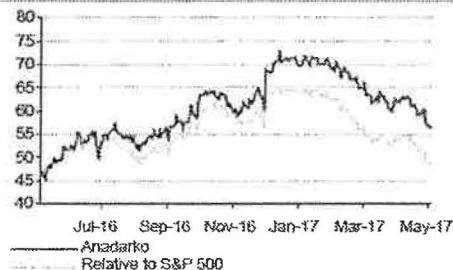
**Anadarko****Shenandoah field write-off overshadows results**

Asset disposals and writedowns added complexity to 1Q earnings. Versus guidance, operating performance was sound but earnings appear soft versus consensus. Optically cash earnings of \$1.84/share missed consensus of \$1.98. A \$1.60/share writedown of Shenandoah was a negative surprise. Separately APC continues to respond to a fatal gas explosion in Colorado linked to one of its well flowlines.

- **Earnings miss in a complex earnings report.** Adjusted EPS of \$(0.60) compares with consensus of \$(0.23) and adjusted cash earnings of \$1.84 were below consensus of \$1.98/share. 1Q results were complicated by asset disposals (Eagle Ford/Marcellus) covering ~20% of group volumes, which closed during the quarter. While guidance excluded divestments, some contributors to consensus may have included these assets.
- **Adjusted sales volumes and cost items in line.** Sales volumes (ex divested assets) were 672kboed, equal to the top of the guidance range. Adjusted onshore US output of 398kboed grew 3% QoQ, as Delaware output climbed with a higher rig count (15 rigs running, +9 YoY). Production costs of \$3.58/boe were below the guidance range of \$3.90-4.10/boe, while other items were broadly in-line. FY17 guidance for total volumes is unchanged and implied guidance on cost items for 2Q-4Q are essentially unchanged. However 1Q tax effects have a knock-on effect on subsequent quarters.
- **Shenandoah write-off.** APC has written-off its Shenandoah project in the deepwater Gulf of Mexico, and taken 1Q charges totalling \$1.4bn (\$2.52/share pre-tax or \$1.60/share post-tax). The move follows an unsuccessful sixth well and subsequent side track which did not find hydrocarbons, putting the scale of the field in doubt. Shenandoah was a high profile discovery which was considered to have potential to be a significant source of new production. Other discoveries reported in the GoM (Calpurnia, Horn Mountain Deep) are modest in scale and will not offset the loss of Shenandoah.
- **Colorado explosion linked to APC well flowline.** Separately to the earnings release, yesterday a Colorado fire dept. report linked a 'cut, abandoned gas flow line', leading from an APC vertical well, to a fatal house explosion outside Denver. The well, drilled by another company in 1993, was acquired by APC in 2014. A statement from APC last night reiterated its commitment to safety, including assessing all 3,000 vertical wells in the area, which it voluntarily shut in following the incident. Volumes affected are ~2% of group output. Of greater importance is community tolerance of oil and gas activities as residential areas spread into existing oil and gas fields.

Ticker (NYSE)	APC
Price	\$56.28
Pricing Date / Time	2 May 2017 / 16:00 ET
Market Capitalisation	\$31,536m
12 Month Range	\$44.81 - \$73.33
YTD Change	-19.3%
Annualised Dividend	\$0.20
Dividend Yield	0.4%
S&P500 YTD Change	6.8%

Price Performance Chart



Y/E Dec	2015A	2016A	2017E
<b>Diluted Cash Flow/Share (\$)</b>			
Q1	2.95	0.96	1.25
Q2	2.53	1.31	1.82
Q3	1.92	1.66	2.00
Q4	1.59	1.93	2.17
FY	9.00	5.86	7.21
<b>Diluted EPS (\$)</b>			
Q1	(0.72)	(1.12)	(0.60)
Q2	0.01	(0.60)	(0.27)
Q3	(0.70)	(0.89)	(0.16)
Q4	(0.58)	(0.49)	(0.03)
FY	(2.00)	(3.09)	(1.05)
P/E (x)	(28.1)	(18.2)	(53.6)

**IMPORTANT DISCLOSURES  
ARE INCLUDED AT THE  
END OF THIS REPORT**

## Anadarko

**1. Shenandoah field write-off overshadows results**

Anadarko's sales volumes were 672kboed in 1Q17, excluding contributions from the Eagle Ford and Marcellus. GAAP volumes were 795kboed (Figure 1). FY16 output from the Eagle Ford was 73kboed (9% of total, 36% oil) and the Marcellus contributed 10% of total output (100% gas).

**Figure 1: 1Q17 sales volumes: reconciliation from pro-forma to reported volumes**

Item	unit	Output adjusted for disposals	Guidance low end	Guidance high end	Adjusted output vs mid- guidance	Reported output	Consensus (5-9 ests)
Total output	kboed	672	656	678	1%	795	690
Crude oil							
US	kbld	255	253	256	0%	269	
Algeria	kbld	70	70	71	-1%	70	
Ghana	kbld	28	28	29	-2%	28	
Total	kbld	353	351	356	0%	367	360
Natural gas							
US	MMscfd	1,275	1,260	1,300	0%	1,859	1,365
Natural gas liquids							
US	kbld	100	96	100	2%	112	
Algeria	kbld	6	5	7	0%	6	
Total	kbld	106	101	107	2%	118	106

Source: Company, Bloomberg consensus

We calculate cash earnings of \$1.84/share versus consensus of \$1.98 (Figure 2). Importantly, we have reversed a \$323m (\$0.59/share) tax charge on profits from the disposals in our calculation.

**Figure 2: Reconciliation of cash earnings per share to GAAP cash from operations**

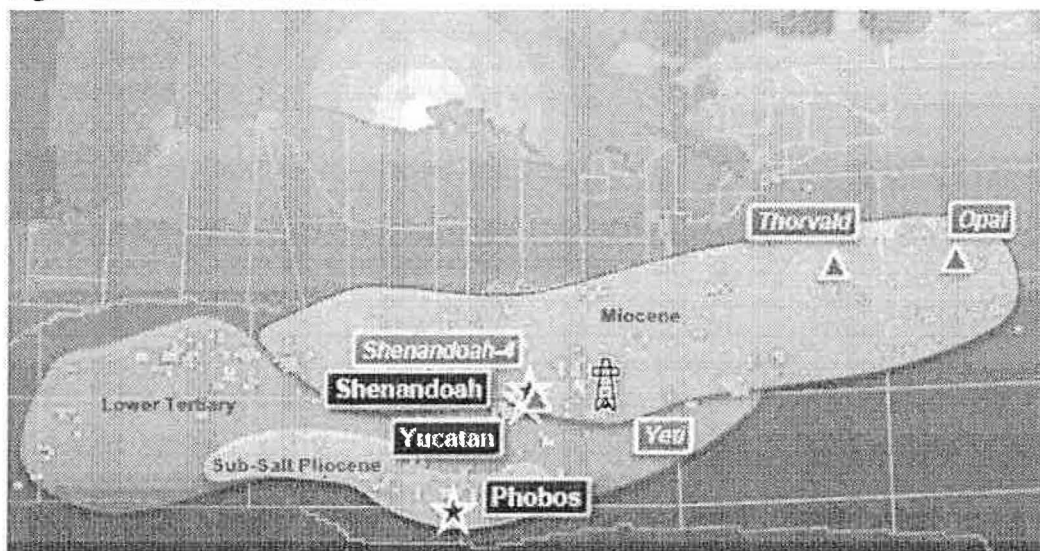
\$m, except per-share	1Q17	1Q16
GAAP net cash from operations	1,123	-137
Add back:		
Increase (decrease) in accounts receivable	-68	-46
(increase) decrease in a/c payable and current liabilities	-395	326
Tax on asset sale profits	323	0
Other	29	343
Adjusted cash flow from operations (cash earnings)	1,012	486
Adjusted cash earnings per share	1.84	0.95

Source: Company, Atlantic Equities calculations

The halt of appraisal activity and associated write-down of Shenandoah investments (Figure 3) is likely to be seen as disappointing. Shenandoah was previously described by APC in 2015 as advancing towards development, and a production concept (semi-sub) had been selected. However the recently drilled Shenandoah #6 well and associated sidetrack failed to find hydrocarbons, leading to the abandonment of the project.



Figure 3: Shenandoah location



Source: Company. Yellow area are APC blocks

Shenandoah was discovered in 2009 as part of a wave of sub-salt, lower Tertiary discoveries. What set Shenandoah apart was apparently much higher reservoir quality than other fields of a similar age. The reservoir is at 30,000ft total depth in 5,750 ft of water. Appraisal wells found over 1,000ft of net oil pay, unusually thick for the Gulf of Mexico. However the field is structurally and depositionally complex, requiring much appraisal drilling to fully understand the reservoir dynamics.

Figure 4: Sales volumes YoY comparison

	1Q16A	1Q17A	YoY change (%)
<b>Crude Oil and Condensate Sales Volumes (kbld)</b>			
United States	232	269	16%
Algeria	65	70	8%
Other	18	28	56%
Total consolidated operations	315	367	17%
<b>Crude Oil and Condensate Realised Prices (\$/bl)</b>			
United States	28.04	49.23	76%
Algeria	34.62	53.20	54%
Other	32.27	53.77	67%
Consolidated average realized prices	29.64	50.34	70%
<b>US Natural Gas Sales Volumes (MMcfd)</b>			
United States	2303	1,859	-19%
<b>Natural Gas Realised Prices (\$/Mcf)</b>			
United States	1.75	3.00	71%
<b>US Natural Gas Liquids Sales Volumes (kbld)</b>			
United States	122	112.00	-8%
<b>US Natural Gas Liquids Realized Prices (\$/Bbl)</b>			
United States	14.98	26.57	77%
Total sales, continuing consolidated operations (kboed)	827	795	-4%

Source: Company

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Figure 5: Income statement YoY comparison

	1Q16A	1Q17A	YoY change (%)
<b>Income statement (\$m)</b>			
E&P Revenues	1394	2,454	76%
Gathering, processing and marketing sales	240	444	85%
Other	40	869	nm
Expenses:			
Direct production expenses	208	258	24%
Oil and gas transportation and other	242	249	3%
Exploration	126	1085	761%
Gathering, processing, and marketing	215	351	63%
General and administrative	449	269	-40%
Depreciation, depletion, and amortization	1149	1115	-3%
Other taxes	117	155	32%
Impairments	16	373	2231%
Tax and legal settlements, other	16	22	nm
Total operating expenses	2538	3877	53%
Operating Income	-864	-110	-87%
Interest, net of amount capitalized	220	223	1%
(Gain) loss on commodity derivatives	297	-147	-149%
Other non-operating (income) expense, net	0	-8	nm
Total other (income) expense	517	68	-87%
Income before Income Taxes	-1381	-178	-87%
Income Tax Provision (Benefit)	-383	97	-125%
Income from Continuing Operations	-998	-275	-72%
Minorities	36	43	19%
Net Income	-1034	-318	-69%
Adjusted net income, continuing operations	-569	-330	-42%

Source: Company

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Figure 6: Operating, financial summary

	1Q17	2Q17E	3Q17E	4Q17E	2016	2017E	2018E	2019E	2020E
<b>Production</b>									
Oil (kbld)	367	335	359	384	316	361	409	447	497
Natural gas (MMscfd)	1,859	1,250	1,100	1,000	2,094	1,302	1,342	1,517	1,750
NGLs (kbld)	118	99	99	101	128	104	105	122	139
Total production (kboed)	795	642	641	652	793	683	738	822	928
<b>Price benchmarks</b>									
Brent oil (\$/bl)	54.60	57.00	57.00	57.00	44.87	56.40	67.00	77.00	78.50
WTI oil (\$/bl)	51.77	55.00	55.00	55.00	43.30	54.19	65.00	75.00	76.50
Natural gas (Henry Hub, \$/MMBtu)	3.06	3.00	3.00	3.00	2.55	3.02	3.00	3.00	3.00
<b>Price realisations</b>									
Oil (\$/bl)	50.34	53.19	53.09	53.02	40.23	52.41	63.10	73.04	74.46
Natural gas (\$/MMBtu)	3.00	2.70	2.70	2.70	2.25	2.78	2.85	2.85	2.85
NGLs (\$/bl)	27.17	22.49	22.49	22.47	19.87	23.63	27.04	27.79	28.04
<b>Income statement (\$m)</b>									
E&P Revenues	2,454	2,131	2,231	2,330	7,153	9,147	11,859	14,735	16,805
Other revenues	1,313	375	423	474	716	2,585	1,848	1,934	2,025
Direct production expenses	-258	-234	-236	-240	-811	-968	-1,100	-1,285	-1,500
Transportation, other	-249	-205	-207	-210	-1,002	-870	-989	-1,145	-1,349
Exploration	-1,085	-165	-165	-165	-946	-1,580	-1,544	-1,606	-1,670
Gathering, processing, marketing	-351	-255	-303	-354	-1,087	-1,263	-1,368	-1,450	-1,535
General and administrative	-269	-263	-266	-270	-1,440	-1,067	-1,239	-1,425	-1,614
D,D&A	-1,115	-1,038	-1,047	-1,064	-4,301	-4,264	-4,715	-5,399	-6,455
Other taxes	-155	-149	-156	-163	-536	-623	-889	-1,105	-1,260
Impairments	-373	0	0	0	-227	-373	0	0	0
Tax and legal settlements	-22	0	0	0	-118	-22	0	0	0
Operating income	-110	198	275	338	-2,599	701	1,864	3,254	3,447
Net interest expense	-223	-225	-215	-200	-890	-863	-806	-750	-690
Other	155	0	0	0	-340	155	8	8	8
Pretax income	-178	-27	60	138	-3,829	-7	1,066	2,512	2,766
Effective tax rate	4%	-138%	108%	65%	31%	-2798%	58%	49%	48%
Minorities	-43	-85	-87	-66	263	281	295	310	326
Attributable reported net income/(loss)	-318	-149	-92	-18	-3,071	-577	156	973	1,108
Attributable recurrent net income/(loss)	-330	-149	-92	-18	-1,604	-589	156	973	1,108
<b>Recurring EPS (diluted, \$)</b>	<b>-0.59</b>	<b>-0.27</b>	<b>-0.16</b>	<b>-0.03</b>	<b>-3.09</b>	<b>-1.05</b>	<b>0.28</b>	<b>1.71</b>	<b>1.93</b>
Share count, weighted diluted (m)	559	559	559	559	522	560	564	570	574
<b>\$/boe items</b>									
E&P Revenue	34.3	36.5	37.8	38.9	24.6	36.7	44.0	49.1	49.5
Direct production expenses	3.6	4.0	4.0	4.0	2.8	3.9	4.1	4.3	4.4
Transportation, other	3.5	3.5	3.5	3.5	3.5	3.5	3.7	3.8	4.0
Exploration	15.2	2.8	2.8	2.8	3.3	6.0	5.7	5.4	4.9
General and administrative	3.8	4.5	4.5	4.5	5.0	4.3	4.6	4.8	4.8
D,D&A	16.0	17.8	17.8	17.8	14.8	17.3	17.5	18.0	19.0
Recurring net income	-4.6	-2.5	-1.6	-0.3	-5.5	-2.4	0.6	3.2	3.3

Source: Company, Atlantic Equities forecasts

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Figure 7: &lt;Insert Figure Title&gt;

\$m except where noted	1Q17	2Q17E	3Q17E	4Q17E	2016	2017E	2018E	2019E	2020E	
<b><u>Discretionary &amp; debt-adjusted cash flow</u></b>										
Net income	-275	-64	-5	48	-2808	-295	451	1283	1434	
Depreciation, depletion, and amortization	1115	1038	1047	1064	4301	4264	4715	5399	6455	
Deferred income taxes	-660	-56	-26	0	-1238	-743	31	162	186	
Dry hole expense, unproved writedowns	1012	100	100	100	613	1312	1366	1420	1477	
Other	-503	0	0	0	1735	-503	0	0	0	
Discretionary cash flow	689	1018	1116	1212	2603	4035	6562	8264	9553	
<b>Discretionary cash flow per share</b>	<b>1.23</b>	<b>1.82</b>	<b>2.00</b>	<b>2.17</b>	<b>5.86</b>	<b>7.21</b>	<b>11.64</b>	<b>14.50</b>	<b>16.65</b>	
<i>YoY growth</i>					-35%	23%	61%	25%	15%	
					<b>FY16-FY20 CFP5 CAGR:</b>					<b>30%</b>
Post-tax interest expenses	145	146	140	130	579	561	524	487	449	
Debt-adjusted discretionary cash flow	834	1164	1256	1342	3182	4596	7086	8752	10001	
Debt-adjusted discretionary cash flow/share (\$)	1.5	2.1	2.2	2.4	7.0	8.2	12.6	15.4	17.4	
YoY growth (%)	21%	31%	16%	9%	-31%	18%	53%	22%	13%	
Total net cash used in investing activities	1722	-1300	-1300	-1300	-3076	-2178	-6048	-6749	-7648	
Cash flow from operations	1123	1223	1080	1176	3000	4603	6571	8210	9597	
Free cash flow	2845	-77	-220	-124	-76	2425	523	1461	1949	
Dividends	-28	-28	-28	-28	-104	-112	-119	-126	-133	
<b><u>Returns and debt metrics</u></b>										
Net debt	9495	9685	10038	10229	12139	10229	10193	9263	7892	
Total equity	11856	11679	11559	11513	12212	11513	11550	12397	13373	
Other	0	0	0	0	0	0	0	0	0	
Capital Employed	21351	21364	21598	21742	24351	21742	21743	21660	21265	
Average capital employed					25950	23047	21742	21701	21462	
Adj. operating profit less taxes (NOPLAT)					-1026	-28	679	1460	1557	
ROACE (%)					-4%	0%	3%	7%	7%	
ROE (%)					-25%	-5%	1%	8%	8%	
Net debt/capitalisation (%)					50%	47%	47%	43%	37%	
Consolidated adjusted EBITDAX	2575	1316	1400	1501	3571	6792	7902	10034	11343	
Consolidated adjusted EBITDA	1490	1151	1235	1336	2625	5212	6358	8429	9673	
Net debt/EBITDAX annualised	0.9	1.8	1.8	1.7	3.4	1.5	1.3	0.9	0.7	
Net debt/EBITDA annualised	2.0	2.5	2.3	2.2	4.6	2.0	1.6	1.1	0.8	

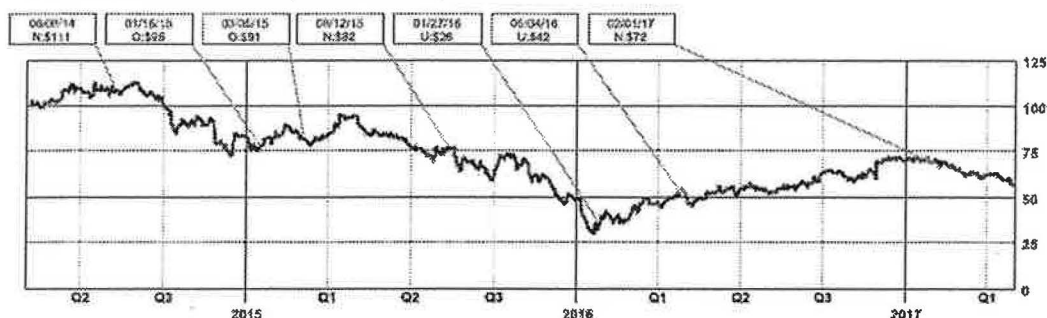
Source: Company, Atlantic Equities forecasts



Anadarko

## IMPORTANT DISCLOSURES

Rating and Price Target History for: Anadarko (APC US) as of 05-02-2017

**Stocks under the analyst's coverage**

Apache (APA), Anadarko (APC), EOG Resources (EOG), Hess (HES), Marathon Oil (MRO), Noble Energy (NBL), Occidental (OXY), Schlumberger (SLB), Baker Hughes (BHI) and Halliburton (HAL).

**Risks**

Potential changes to our Neutral rating on Anadarko may arise from, but are not limited to, changes in commodity prices, operating and capital costs, changes in state and federal tax and regulatory changes, modifications in restrictions on hydraulic fracturing, environmental constraints and per-well productivity.

**Consensus Estimates**

Consensus estimates have been sourced from Bloomberg.

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Barry MacCarthy, hereby certifies that the views expressed in this research report accurately reflects his/her personal views about the subject Security and Issuer as of the date of this report. He/She further certifies that no part of his/her compensation was, is, or will be directly, or indirectly, related to the specific recommendations or views contained in this research report.

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